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No. ~~7221~~ 7

SUPREME COURT OF THE STATE OF WASHINGTON

CHADWICK FARMS OWNERS ASSOCIATION, a Washington
nonprofit corporation

Plaintiff/Appellant,

v.

FHC LLC, a Washington limited liability company,

Defendant/Third Party Plaintiff/Respondent/Cross-Appellant,

v.

AMERICA 1ST ROOFING & BUILDERS, INC., a Washington
corporation; CASCADE UTILITIES, INC., a Washington corporation;
MILBRANDT ARCHITECTS, INC., P.S., a Washington corporation;
PIERONI ENTERPRISE, INC., d/b/a PIERONI'S LANDSCAPE
CONSTRUCTION, a Washington corporation, TIGHT IS RIGHT
CONSTRUCTION, a WASHINGTON corporation; GUTTER KING,
INC., a Washington corporation,

Third Party Defendants/Cross-Respondents.

**BRIEF OF CROSS-RESPONDENT
CASCADE UTILITIES, INC.**

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I. RESTATEMENT OF THE ISSUE

Whether the trial court properly granted Cascade Utilities, Inc.'s (hereinafter, "Cascade") motion for summary judgment based on the fact that once FHC, LLC (hereinafter, "FHC") was cancelled by the Secretary of State, it lost the privilege and power to prosecute claims against the third-party defendants?

II. STATEMENT OF THE CASE

This case is about a limited liability company ("LLC") that failed to file its annual report and pay its license renewal fees and, as result – pursuant to statutory mandate and after written notice – the Secretary of State dissolved the LLC and then cancelled the LLC's formation. Pursuant to statute, when cancellation occurred, the LLC ceased to exist and lost any right or ability to act.

A. The Trial Court Granted the Parties' Motions for Summary Judgment

On September 30, 2005, the trial court granted FHC's motion for summary judgment against Chadwick Farms Owners Association (hereinafter, the "HOA") based on the cancelled status of FHC. CP 208-210. The trial court also granted separate orders dismissing FHC's claims against Cascade, Milbrandt Architects, Inc., P.S., and Pieroni Enterprise,

Inc. based on their summary judgment motions. CP 105-107, 98-101, 108-112.

B. Timeline of Key Events

A relevant timeline of events is as follows:

EVENT	DATE	CITATION
FHC's date of Incorporation	December 23, 1999	CP 84
FHC's Date of Administrative Dissolution	March 24, 2003	CP 13, 84
HOA Filed its Complaint Against FHC	August 18, 2004	CP 119-25
Date of Cancellation of FHC's Certificate of Formation by the Secretary of State	March 24, 2005	CP 2, 84
FHC Filed its Third-Party Complaint Against Cascade, et al.	May 12, 2005	CP 139-52

It is important to note from this timeline that, while the HOA's lawsuit was filed against FHC before FHC was cancelled, FHC's lawsuit against Cascade and the other third-party defendants was filed after FHC was cancelled. The critical importance of this distinction is discussed next.

III. ARGUMENT

A. **At the Outset it is Critical to Note that FHC's Claims against Cascade are *Factually Distinguishable* from the HOA's Claims against FHC**

Though Cascade argues herein and establishes that a cancelled LLC may not prosecute claims, Cascade takes no position as to whether an LLC may defend against claims that were filed prior to cancellation. The factual distinction with respect to the claims in this case allows this Court to provide **different rulings** as between the HOA's claims against FHC versus FHC's claims against Cascade.

As noted above, the HOA's claims were pending prior to FHC's cancellation. Thus, it could be argued that the HOA's claims were known to FHC **prior to** its cancellation and, therefore, FHC had a duty to pay all claims and obligations against it pursuant to RCW 25.15.300(2). That is not the case with FHC's claims against Cascade and the other third-party defendants, which were filed **after** FHC's cancellation.

The question between the HOA and FHC is different (from the issue involving Cascade) because the HOA did not have the ability to maintain FHC's LLC form by, for example, paying FHC's fees to prevent dissolution or paying the fees to reinstate FHC after its dissolution. On the other hand, FHC always had the right and the ability to maintain its privilege to prosecute claims against Cascade, or anyone else, by simply

paying its fees to prevent dissolution or to pay its fees to reinstate FHC after dissolution. FHC knowingly gave up its privilege and power to prosecute claims by voluntarily allowing itself to be cancelled. Set forth next is a brief discussion of the LLC statutory structure and its operation.

B. Cancellation of FHC, LLC's Certificate of Formation Resulted in its Existence, and all its Rights, Being Extinguished: FHC, LLC Cannot Prosecute Claims

An LLC is a creature of statute, specifically, The Washington Limited Liability Company Act (Chapter 25.15 RCW). An LLC is created by statute and derives all rights from a statute. An LLC ceases to exist and loses all rights to act upon the occurrence of certain events specifically outlined by statute. Any rights that FHC asserts that it has in this case, therefore, must be supported by the controlling LLC statutes. If not, those asserted rights simply do not exist.

The facts are undisputed that FHC failed to maintain its standing with the Secretary of State, was administratively dissolved, and then had its certificate of formation cancelled. FHC only disputes the effect of the cancellation of its certificate of formation. FHC finds no support for its arguments, however, in the statutes. It is these same statutes which confirm that FHC ceased to exist and lost all rights/standing to prosecute claims – or otherwise act – when its certificate of formation was cancelled on March 24, 2005.

1. **LLC Protection is a Limited Privilege, Not a Right:
Proper Maintenance of an LLC is Required**

The LLC entity affords its individual members protection from the “debts, obligations, and liabilities of [the] limited liability company, whether arising in contract, tort or otherwise.” RCW 25.15.125. In order to form an LLC, one or more persons must execute a certificate of formation pursuant to RCW 25.15.070(1). In short, an LLC does not exist without a valid certificate of formation:

A limited liability company...shall be a separate legal entity, the existence of which as a separate legal entity shall continue until cancellation of the limited liability company’s certificate of formation.

RCW 25.15.070(2)(c)(emphasis added).

In recognition of the fact that an LLC’s existence, and protection of its members, is a privilege and not a right, our Legislature has imposed several requirements upon an LLC to enjoy the protections of the LLC statute. The requirements that an LLC must meet are simple but mandatory, including the filing of initial and annual reports (which includes a list of officers/managers). RCW 25.15.105. Our Legislature has also empowered the Secretary of State with the administration of limited liability companies. RCW 43.07.030. As explained next, **if an LLC fails to comply with these statutory requirements, the Secretary of State shall – without exception – dissolve and ultimately cancel the**

LLC. Because FHC failed to meet the requirements of the LLC statute, that is exactly what happened.

2. Methods of Cancelling an LLC

An LLC may cease to exist through any one of three ways. First, the members of an LLC may affirmatively voluntarily dissolve and cancel its certificate of formation. RCW 25.15.270; 25.15.080. Second, the superior courts may judicially dissolve and cancel an LLC on application by any member. RCW 25.15.275; 25.15.295; 25.15.090. Third, the Secretary of State may commence a proceeding to administratively dissolve and cancel an LLC where, as here, the LLC fails to file the necessary reports. RCW 25.15.280; 25.15.085; 25.15.290. As this case involves the administrative dissolution and cancellation of FHC, this brief focuses only on this third way by which an LLC's certificate of formation is cancelled.

3. Administrative Dissolution and Cancellation of LLC

The Secretary of State commences a proceeding to administratively dissolve an LLC upon the occurrence of certain events. One such event triggering dissolution is where the LLC fails to properly file its annual report – as we have here. RCW 25.15.280. If the Secretary of State determines that such a ground exists for administrative dissolution, “the secretary of state shall give the limited liability company

written notice of the determination.” RCW 25.15.285(1). Thereafter, “[a] limited liability company administratively dissolved under RCW 25.15.285 may apply to the secretary of state for reinstatement within two years after the effective date of dissolution.” RCW 25.15.290(1).

If an application for reinstatement is timely made and if the Secretary of State determines it to be sufficient, the LLC is reinstated and it “may resume carrying on its business as if the administrative dissolution had never occurred.” RCW 25.15.290(3). However,

If an application for reinstatement is not made within the two-year period..., or if the application made within this period is not granted, the secretary of state shall cancel the limited liability company’s certificate of formation.

RCW 25.15.290(4) (emphasis added). This statutorily mandated cancellation of the LLC’s certificate of formation is the same result achieved by the voluntary filing of a certificate of cancellation (which relates to voluntary and judicial dissolution). RCW 25.15.080.

4. No Exception if LLC Fails to File Annual Report

It is important to recognize that if an LLC fails to file the annual report/pay license fees, there is no exception and the LLC will be dissolved and, if not reinstated, cancelled at the end of the two-year period. That is, regardless of any other action and even if an LLC is in the midst of pursuing dissolution and cancellation via the voluntary or judicial

process, once an LLC fails to file its annual report, the administrative dissolution process is commenced. Only a properly filed and accepted application for reinstatement – pursuant to RCW 25.15.290(1) – may remove the LLC from this involuntary administrative cancellation process. Thereafter, cancellation of the limited liability’s certificate of formation is its statutory death knell:

A limited liability company...shall be a separate legal entity, the existence of which as a separate legal entity shall continue until cancellation of the limited liability company’s certificate of formation.

RCW 25.15.070(2)(c)(emphasis added).

5. An Administratively Dissolved LLC has Only Limited Authority to Act Prior to its Cancellation

An administratively dissolved LLC continues to exist only to “wind up” and liquidate its business and affairs. RCW 25.15.285(3). As part of the winding up process, the LLC may “prosecute and defend suits..., [and] gradually settle and close the limited liability company’s business.” RCW 25.15.295(2). As discussed next, however, the Legislature expressly limited the duration of the dissolved LLC’s “winding up” period and its right to otherwise act.

6. **Cancelled LLC Loses All Rights/Standing to Act,
Including Right to Prosecute Claims**

The Legislature limited the administratively dissolved LLC's winding up period to a maximum of two years, thereby extinguishing the LLC's rights to act simultaneously with its cancellation:

A limited liability company is dissolved and its affairs shall be wound up upon the first to occur of the following:

(6) The expiration of two years after the effective date of administrative dissolution without the reinstatement of the limited liability company.

RCW 25.15.270(6) (emphasis added). This is consistent with the provision of the statute authorizing the limited liability to wind up only "until the filing of a certificate of cancellation as provided in RCW 25.15.080." Further, RCW 25.15.080 specifically includes the statutorily mandated cancellation of the LLC's certificate of formation where it fails to reinstate within two years of the date of administrative dissolution. RCW 25.15.290(4); see also RCW 25.15.080. Simply stated, Chapter 25.15 RCW allows an administratively dissolved LLC to wind up only until its certificate of formation is cancelled.

The foregoing is equally consistent with the LLC statutory scheme that mandates that an LLC can only exist – and, therefore, can only act – if it maintains a valid certificate of formation. RCW 25.15.070. Once an

LLC's certificate of formation is cancelled, the LLC ceases to exist for any and all purposes and its power to act is extinguished. *Id.*

7. FHC was Cancelled, Extinguishing its Right to Prosecute Claims Against Cascade Utilities, *et al.*

In this case, FHC was administratively dissolved on March 24, 2003 for failure to file its annual report. CP 13, 84. FHC did not apply for reinstatement. Therefore, pursuant to statute, two years later the Secretary of State cancelled FHC's certificate of formation. CP 83-87. These critical facts are not disputed. As a result, FHC's winding up period ended – and it ceased to exist as a legal entity – on March 24, 2005.

It is important to note that FHC always retained the exclusive power and authority – prior to cancellation – to preserve its LLC form and maintain its right to continue to conduct business and to prosecute claims. FHC needed only to submit an application for reinstatement to the Secretary of State within two years of administrative dissolution. FHC, therefore, always controlled its own destiny in this matter. **FHC voluntarily chose, however, to allow its formation to be cancelled.** By mandatory statute, on March 24, 2005, FHC ceased to exist and lost its power to prosecute claims. RCW 25.15.270(6); RCW 25.15.295(2).

8. “Winding Up” Period *Limited, Not Indefinite*

An LLC cannot exist, and cannot act, in perpetuity. Once FHC’s certificate of formation was cancelled, it ceased to exist and could no longer do anything.

FHC was administratively dissolved on March 24, 2003. CP 13, 84. On that date, the clock started ticking on FHC’s winding up period. Pursuant to RCW 25.15.270, the winding up period must conclude within two years of the date of administrative dissolution. The statute states, “A limited liability company is dissolved and its affairs shall be wound up upon...the expiration of two years after the effective date of [administrative] dissolution.” RCW 25.15.270. With the use of the term “shall,” the legislature rendered the time limitation mandatory. FHC’s affairs shall be wound up within two years of the date of administrative dissolution – i.e., March 24, 2005. FHC may not continue to wind up beyond March 24, 2005, which includes prosecuting claims. RCW 25.15.270. FHC filed its third-party complaint on May 12, 2005. CP 139-52.

Because FHC’s winding up period was over and the Secretary of State cancelled its certificate of formation, FHC lacked standing to prosecute claims against the third-party defendants. If FHC wanted to preserve its right to prosecute claims, it should have reinstated with the

two year time period set forth in RCW 25.15.290(1). FHC did not reinstate within the applicable time period, and therefore lacks standing to prosecute claims after cancellation.

9. LLC Statute Must be Construed to Give Administrative Dissolution Provisions Effect, Not Render them Meaningless

Any interpretation of Chapter 25.15 RCW to extend the winding up period indefinitely would render meaningless the act of administrative dissolution of an LLC altogether. “A court...must construe statutes such that all of the language is given effect, and no portion is rendered meaningless or superfluous.” Restaurant Development, Inc. v. Cananwill, Inc., 150 Wn.2d 674, 682, 80 P.3d 598 (2003) (en banc) (citations omitted). If an administratively dissolved LLC were permitted to continue into perpetuity, what incentive would it have to file its annual reports as required by RCW 25.15.105? What incentive would it have to apply for reinstatement upon notice of administrative dissolution (as required by RCW 25.15.290)? As noted earlier, the privileges bestowed upon an LLC pursuant to the LLC statutes require that an LLC meet certain minimal requirements – such as filing an annual report – to maintain its LLC form. If it fails to meet these requirements, it is cancelled – **no exceptions** – as FHC was here.

10. LLC Not Required to Take Affirmative Action to Result in Cancellation after Administrative Dissolution

It is important to bear in mind that the LLC statutes do not require any affirmative action by the administratively dissolved LLC to effect cancellation or end its wind up period (i.e. said LLC does not need to file a Certificate of Cancellation). The Secretary of State automatically cancels an LLC's certificate of formation if – as here – no reinstatement application is made within two years of administrative dissolution. RCW 25.15.290(4). The LLC administrative dissolution and cancellation statutes recognize that the administratively dissolved LLC has, in effect, been abandoned. A statutorily mandated cancellation is warranted. It would be unreasonable to rely upon the administratively dissolved LLC to file its own Certificate of Cancellation, as the LLC's disregard for the filings required by Chapter 25.15 RCW led to the administrative dissolution in the first place.

11. Washington Law Bars Absurd Result

Washington courts “avoid reading of statutes that result in unlikely, absurd, or strained consequences.” Advanced Silicon Materials, LLC v. Grant County, 124 P.3d 294, 297 (2005) (en banc) (citations omitted). In that vein, it would be an absurd result to allow an LLC that fails/refuses to comply with its statutorily required duties to exist in perpetuity. That is, if an administratively dissolved LLC cannot be

cancelled by the Secretary of State without affirmative action taken by the LLC (i.e. filing a certificate of cancellation), how would the non-responsive LLC **ever** be wound up and cancelled? The answer is that such an LLC would never be cancelled and would continue in perpetuity. The LLC statute, itself, precludes such an absurd result.

12. Undisputed Fact that Secretary of State Cancelled FHC, LLC's Formation

As mandated by statute, on March 24, 2005, FHC ceased to exist and lost its power to prosecute claims. RCW 25.15.270(6); RCW 25.15.295(2). This was confirmed via declaration by a representative of the Washington Secretary of State, which included the following information:

- Pursuant to RCW 25.15.290, FHC LLC had two years from the date of administrative dissolution within which to apply for reinstatement;
- FHC LLC did not apply for reinstatement following the filing of the Certificate of Administrative Dissolution;
- Pursuant to RCW 25.15.290(4) and because no application for reinstatement was received by the secretary of state from FHC LLC within two years of the date of administrative dissolution, the secretary of state cancelled FHC LLC's certificate of formation on March 24, 2005; *and*

• The cancellation of the certificate of formation terminated FHC LLC's winding up period and the Secretary of State considered FHC LLC "dead" as of March 24, 2005.

CP 83-87.¹

C. Cascade's Right to a Dismissal of FHC's Action Based on FHC's Cancellation is Independent, and Distinguishable, From the Issues Involving the HOA: Different Rulings are Warranted

Assuming that the HOA's claims against FHC are allowed to proceed, such a result should have no impact on barring FHC's claims against Cascade. Despite FHC's assertions to the contrary, the factual and legal distinctions based on the timing of the claims and FHC's cancellation – as well as the impact of same pursuant to the LLC statute – creates a factual and legal basis for this Court to issue different rulings as to the HOA's claims against FHC and FHC's claims against Cascade, *et al.* As outlined above, the law bars a cancelled LLC from prosecuting claims. It cannot be argued that this is an unfair or harsh result, as the power to retain the privilege of prosecuting claims lied solely with FHC itself. FHC easily could have preserved its right to prosecute claims – and

¹ It is important to note that the Secretary of State's declaration, and the evidence therein, is *undisputed fact*. In said declaration, the Secretary of State testified and confirmed that "the secretary of state cancelled FHC, LLC's certificate of formation on March 24, 2005." CP 83-87. Therefore, FHC's cancellation is undisputed fact that bars FHC (because it now has no standing in this Court) from disputing the Secretary of State's decision to cancel FHC. Thus, the only possible issue is the *effect* of that cancellation.

could have avoided the cancellation of its certificate of formation – by applying for reinstatement pursuant to RCW 25.15.290. It did not do so.

Any harsh result that may exist by dismissing the HOA's claims has no bearing on FHC's claims against Cascade. Though the HOA may have done everything it could do to preserve its claims, FHC did nothing to preserve its claims against Cascade, et al. FHC needed only to submit an application for reinstatement to the Secretary of State within two years of administrative dissolution. FHC, therefore, always controlled its own destiny in this matter. In fact, the HOA sued FHC prior to the expiration of the two year reinstatement period. Clearly FHC made the choice to allow its formation to be cancelled and waive its LLC privileges and the power to prosecute claims.

D. Senate Bill 6531 Does Not Revive FHC's Ability to Prosecute Claims

The recently enacted legislation found in Senate Bill 6531 does not change the law with respect to an administratively dissolved LLC's right to prosecute claims nor any other affirmative rights of the LLC to act. Instead, these rights are extinguished (as are all winding up activities) upon cancellation of the certificate of formation. The proposed statute merely seeks to preserve the claims against a cancelled LLC, but not preserve the LLC's own right to pursue claims. This is evidenced by the

language in the legislation itself, which addresses remedies available **against** an LLC, and sets forth a three year time period in which an action must be commenced **against** that LLC. SB 6531. The bill is silent, however, as to an LLC's ability to prosecute claims. Therefore, all rights to prosecute claims would remain as outlined in RCW Ch. 25.15.

Here, the bottom line is that FHC had two years of opportunity to reinstate and preserve its rights to prosecute claims. FHC chose to do nothing. FHC cannot now complain that it was cancelled and that all its rights to act – and prosecute claims – were extinguished.

E. FHC's Notice of Appeal was not Timely Filed

A notice of appeal from an order granting a motion for summary judgment must be filed in the trial court within 30 days after entry of the decision of the trial court which the party filing the notice wants reviewed.

RAP 5.2(a). In this case, the order granting Cascade's Motion for Summary Judgment was entered on September 30, 2005. CP 105-07. FHC's Notice of Appeal of that order was filed on or about January 12, 2006, more than 90 days after entry of the order FHC wanted reviewed. CP 276-300.

FHC attempts to confuse the issue by pointing to dismissals of two additional parties entered in November and December of 2005. Those dismissals, however, are irrelevant to this appeal. The voluntary

dismissals are not orders on which FHC seeks review. Furthermore, while those parties had not joined in the summary judgment motion at issue in this appeal, the trial court's order granting the third-party defendants' motion for summary judgment was dispositive of the claims against the remaining third-party defendants as well. The summary judgment dismissal of the claims against Cascade Utilities, Inc., Milbrandt Architects, Inc. P.S., and Pieroni Enterprise, Inc. d/b/a Pieroni's Landscape Construction, Inc., effectively disposed of all the claims against as to the third-party defendants.

FHC failed to move for an extension of time in which to file its notice of appeal pending the dismissal of the additional parties not involved in the summary judgment hearing. Further, FHC fails to point to any exceptional circumstances that would warrant a waiver of the rules. Because FHC's notice of appeal was untimely, this Court should not entertain arguments as to FHC's ability to prosecute claims against the third-party defendants.

IV. CONCLUSION

For the reasons set forth herein, the trial court did not err in granting the third-party defendants' motions for summary judgment. Upon cancellation, FHC lost its right to prosecute the third-party claims.

This result could have been prevented if FHC had applied for reinstatement during the applicable time period. It did not do so.

Further, because of the factual distinction between the HOA's pending claims at the time of FHC's cancellation and the post-cancellation prosecution of claims against the third-party defendants, grounds do exist for this Court to provide different rulings as to the HOA's claims against FHC and FHC's claims against the third-party defendants.

RESPECTFULLY SUBMITTED this 2nd day of June, 2006.

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CERTIFICATE OF SERVICE

The undersigned certifies under the penalty of perjury under the laws of the State of Washington that I am now and at all times herein mentioned, a citizen of the United States, a resident of the State of Washington, over the age of eighteen years, not a party to or interested in the above-entitled action, and competent to be a witness herein.

06 JUL -2 3 PM '94
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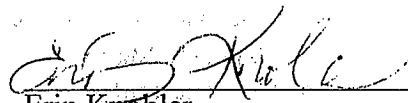
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